

January 22, 2018

EDWARD J. EMMONS, CLERK

U.S. BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

Signed and Filed: January 22, 2018



*Dennis Montali*

DENNIS MONTALI

U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT  
FOR THE NORTHERN DISTRICT OF CALIFORNIA

In re	)	Bankruptcy Case
	)	No. 17-10080-DM
AARON HUGH BRAUN,	)	
	)	Chapter 7
	)	
Debtor.	)	
	)	
CADOGAN MANAGEMENT, LLC,	)	
	)	Adv. Proc. No. 17-03024
Plaintiff,	)	
	)	
v.	)	
	)	
AARON HUGH BRAUN,	)	
	)	
	)	
Defendant.	)	

MEMORANDUM DECISION ON PLAINTIFF'S  
MOTION FOR PARTIAL SUMMARY JUDGMENT

On November 17, 2017, this court held a hearing on the motion for partial summary judgment ("MSJ") filed by plaintiff Cadogan Management, LLC ("Cadogan"), contending that a state court judgment owed to it by defendant and debtor Aaron Hugh Braun ("Debtor") is nondischargeable. Cadogan asserted that the state court judgment precludes Debtor from disputing and litigating the nondischargeability of the resulting judgment debt.

1       At the hearing, this court raised the issue of whether the  
2 state court had "necessarily decided" the issues underlying the  
3 state court judgment, an essential element for the application of  
4 issue preclusion. In particular, the facts alleged in the state  
5 court complaint supported multiple claims, including breach of  
6 contract against Debtor's co-defendants. Cadogan filed a  
7 supplemental brief; Debtor did not. Having considered the  
8 pleadings and the supplemental briefing, and for the reasons set  
9 forth below, the court will grant partial summary judgment in favor  
10 of Cadogan.

11 I.    UNDISPUTED FACTS

12       A.   Claims Asserted Against Debtor in the State Court Action

13       In 2001, Cadogan filed an action against Debtor, Willow Creek  
14 Short Biased 30/130 Fund, L.P. ("WC Fund"), and WC Capital  
15 Management, LLC ("WC Management") in the Marin County Superior  
16 Court (the State Court Action"). The first four causes of action  
17 of the complaint ("State Court Complaint") alleged breach of  
18 contract against WC Management only. The fifth cause of action  
19 asserted breach of fiduciary duty against WC Management and Debtor  
20 and the sixth cause of action asserted conversion against all  
21 defendants. See Cadogan's Request for Judicial Notice ("RJN") at  
22 Docket 16-1, Exhibit A.

23       The seventh cause of action asserted trespass to chattels  
24 against all defendants, alleging that they had

25           not only failed and refused to refund the Remaining  
26 Balance, they have also used the Remaining Balance to  
27 fund an unauthorized trading scheme for their own  
28 benefit. In so doing, Defendants have wrongfully  
exercised dominion and control over the Remaining  
Balance, and misappropriated such funds to their own use.

1 See Cadogan's RJN at Docket 16-1, Exhibit A at paragraphs 51-53.

2 The eighth, ninth and tenth causes of action sought an  
3 accounting, the imposition of a constructive trust, and injunctive  
4 relief against all defendants. See Cadogan's RJN at Docket 16-1,  
5 Exhibit A at paragraphs 51-53.

6 B. Factual Allegations Supporting Claims Against Debtor in  
7 the State Court Action

8 Paragraphs 5-8 of the State Court Complaint describe the  
9 transactions giving rise to Cadogan's claims: the failure of WC  
10 Funds to return balances in certain capital accounts to which  
11 Cadogan was contractually entitled. See Cadogan's RJN at Docket  
12 16-1, Exhibit A at paragraphs 5-8. According to paragraph 8, the  
13 balance which WC Management was contractually required to remit to  
14 Cadogan was \$1,266,549.50, excluding interest (the "Remaining  
15 Balance"). The last sentence of paragraph 8 provides a preview of  
16 the claims against Debtor individually: "On information and belief,  
17 WC Management and Braun [Debtor] misappropriated the Remaining  
18 Balance and used these funds to continue trading for their own  
19 benefit and/or for the benefit of WC Fund, in derogation of their  
20 duties to Cadogan Funds." *Id.*

21 Paragraphs 9-12 of the State Court Complaint describe the  
22 purported misappropriation of the Remaining Balance by Debtor and  
23 the other defendants. In particular, paragraph 11 alleges that  
24 "Defendants, and each of them, used the remaining balance of the  
25 Cadogan Funds' capital accounts to continue trading. . . .  
26 Defendants' unauthorized trading resulted in substantial losses  
27 [reducing the Remaining Balance from \$1,266,549.50 to \$850,000]."  
28 *Id.* at ¶¶ 11-12 (emphasis added).

1        In the allegations supporting its fifth cause of action (for  
2 breach of fiduciary duty) against Debtor individually, Cadogan  
3 asserted that Debtor acted as the manager of WC Management and  
4 portfolio manager of WC Funds and thus owed fiduciary duties to WC  
5 Funds's limited partners, including Cadogan. *Id.* at ¶ 39. Cadogan  
6 further alleged that Debtor knowingly breached those fiduciary  
7 duties by using the Remaining Balance to continue trading instead  
8 of turning them over to it. *Id.* at ¶ 40. "As the manager of WC  
9 Management and portfolio manager of WC Fund, it was [Debtor's]  
10 duty to ensure that WC Management held the Remaining Balance until  
11 such time as it could be returned to the Cadogan Funds. [Debtor]  
12 failed to discharge this duty. Instead, [Debtor] embarked on a  
13 course of unauthorized trading, in breach of [Debtor's] fiduciary  
14 duties to the Cadogan Funds." *Id.*

15        Similarly, in support of its sixth cause of action  
16 (conversion), Cadogan alleged in paragraph 46 of the State Court  
17 Complaint that the defendants (including Debtor) "not only failed  
18 and refused to refund the Remaining Balance, they have also used  
19 the Remaining Balance to fund an unauthorized trading scheme for  
20 their own benefit. In so doing, Defendants have wrongfully  
21 exercised dominion and control over the Remaining Balance, and  
22 misappropriated such funds to their own use." *Id.* at ¶ 46.

23        Likewise, in support of the seventh cause of action for  
24 trespass to chattels against Debtor and the other state court  
25 defendants, Cadogan re-asserted the foregoing factual allegations  
26 and further alleged that Debtor "intentionally took possession of  
27 the Remaining Balance and prevented Cadogan from exercising the  
28 rights and benefits associated therewith." *Id.* at ¶ 40.

1 Finally, as remedies to the torts alleged against Debtor and  
2 the other defendants, Cadogan realleged the foregoing facts and  
3 sought an accounting (the eighth cause of action), the imposition  
4 of a constructive trust (the ninth cause of action) and injunctive  
5 relief (the tenth cause of action). *Id.* at ¶¶ 54-66.

6 C. The State Court Judgment

7 On August 2, 2011, Cadogan filed an Application for Court  
8 Judgment ("Default Application") in state court setting forth the  
9 facts alleged in the State Court Complaint, as well as supporting  
10 declarations and exhibits. See Cadogan's RJN at Docket 16-1,  
11 Exhibit B. The state court thereafter entered a judgment in favor  
12 of Cadogan and against Debtor upon the Default Application "and  
13 having considered the evidence." *Id.* at Exhibit C. Debtor filed  
14 his chapter 7 case on February 8, 2017.

15 D. Admissions by Debtor in this Adversary Proceeding

16 Cadogan's complaint initiating this adversary proceeding (the  
17 "AP Complaint") alleges that WC Fund was a hedge fund established  
18 to manage investments by Cadogan and that WC Management was the  
19 general partner of WC Fund. AP Complaint at Docket No. 1, ¶ 6. It  
20 further alleges that Debtor was the manager of WC Management and  
21 the portfolio manager of WC Fund "and, in fact exercised total and  
22 complete executive control and power over WC Management and WC  
23 Fund." *Id.* at ¶ 7. In his answer filed on May 15, 2017, Debtor  
24 admits both allegations. See Answer, Docket No. 9, ¶ 4.

25 Paragraph 8 of the Complaint alleges that between May 1, 2008  
26 and April 1, 2009, Cadogan made several investments in the WC Fund.  
27 Each was made pursuant to the WC Fund's First Amended and Restated  
28 Agreement of Limited Partnership ("Partnership Agreement") and the

1 WC Fund Confidential Offering Circular (the "Offering Circular" or  
2 "OC"). AP Complaint at Docket No. 1, ¶ 8.

3 Paragraphs 9 and 10 of the Complaint further allege that the  
4 Partnership Agreement expressly provided that (1) as general  
5 partner of WC Fund, WC Management had a fiduciary duty to Cadogan,  
6 and (2) that Debtor was the manager of WC Management and the  
7 portfolio manager of WC Fund. *Id.* at ¶ 9-10. Debtor admitted  
8 these allegations of paragraphs 8, 9 and 10 of the Complaint. *See*  
9 Answer, Docket No. 9, ¶ 4.

10 Most importantly, Debtor admitted the allegations of paragraph  
11 10 of the Complaint:

12 The Partnership Agreement also expressly provides that  
13 [Debtor] was the Manager of the limited liability  
14 corporation, WC Management, and the portfolio manager of  
15 the limited partnership, WC Fund. As Manager of WC  
16 Management and portfolio manager of WC Fund, [Debtor] had  
17 a fiduciary duty to Cadogan.

18 *See* AP Complaint at Docket No. 1, ¶ 10; Answer, Docket No. 9, ¶ 4.

19 II. DISCUSSION

20 Under the Federal Full Faith and Credit Statute (28 U.S.C. §  
21 1738), "a federal court must give to a state-court judgment the  
22 same preclusive effect as would be given that judgment under the  
23 law of the State in which the judgment was rendered."; 28 U.S.C. §  
24 1738; *Migra v. Warren City School Dist. Bd. of Educ.*, 465 U.S. 75,  
25 81 (1984); *Marrese v. Am. Acad. of Orthopaedic Surgeons*, 470 U.S.  
26 373, 380 (1985). Thus, the claims brought by Cadogan are subject  
27 to California's principles of issue and claim preclusion. *Id.*;  
28 *Allen v. McCurry*, 449 U.S. 90, 97-98 (1980) (preclusive effect in  
federal court of state proceedings is same as that accorded in  
state's own courts).

1 Issue preclusion (often called "collateral estoppel")  
2 forecloses relitigation of matters that have already been decided  
3 in prior proceedings. *Paine v. Griffin (In re Paine)*, 283 B.R. 33,  
4 39 (9th Cir. BAP 2002); see also *Harmon v. Kobrin (In re Harmon)*,  
5 250 F.3d 1240, 1245 (9th Cir.2001)(applying California law),  
6 quoting *Lucido v. California*, 51 Cal.3d 335, 272 Cal.Rptr. 767, 795  
7 P.2d 1223, 1225 (1990); Christopher Klein, et al, Principles of  
8 Preclusion & Estoppel in Bankruptcy Cases, 79 Am. Bankr.L.J. 839,  
9 852 (2005). For issue preclusion to apply, the following elements  
10 must be satisfied:

11 First, the issue sought to be precluded from relitigation  
12 must be identical to that decided in a former proceeding.  
13 Second, this issue must have been actually litigated in the  
14 former proceeding. Third, it must have been necessarily  
15 decided in the former proceeding. Fourth, the decision in the  
16 former proceeding must be final and on the merits. Finally,  
17 the party against whom preclusion is sought must be the same  
18 as, or in privity with, the party to the former proceeding.

19 *Harmon*, 250 F.3d at 1245. To conclude that the issue was  
20 "necessarily decided," the issue must not have been "entirely  
21 unnecessary" to the judgment in the prior proceeding. *Lucido v.*  
22 *Superior Court*, 51 Cal.3d 335, 341, 342 (1990). As the Ninth  
23 Circuit held in *Clark v. Bear Stearns & Co.*, 966 F.2d 1318, 1320  
24 (9th Cir. 1992), for issue preclusion to apply, the determination  
25 of an issue in the prior litigation must have been a critical and  
26 necessary part of the judgment in the earlier action.

27 As the court noted at the hearing on November 17, Cadogan  
28 established all but one of the foregoing elements to the court's  
satisfaction. The court questioned, however, whether the state  
court had necessarily decided the breach of fiduciary duty and  
other tort claims as the facts alleged could have supported the

1 "lesser included counts" such as breach of contract. But the  
2 breach of contract claim was not pled against Debtor; the causes of  
3 action pled against him consisted of breach of fiduciary duty as  
4 well as other torts. Thus the entry of the judgment necessarily  
5 required a determination that Debtor owed a fiduciary duty to  
6 Cadogan, that he breached that fiduciary duty and that Cadogan was  
7 damaged by that breach.

8 Even in the absence of the state court judgment, Debtor's  
9 admissions to paragraphs 6-10 to the AP Complaint demonstrate that  
10 he owed a fiduciary duty to Cadogan that arose separate from and  
11 prior to the commission of the alleged wrongdoing. Those  
12 paragraphs allege a fiduciary duty that arose prior to the  
13 wrongdoing: one that was contractual in nature,  
14 arising from WC Fund's First Amended and Restated Agreement of  
15 Limited Partnership and the WC Fund Confidential Offering Circular.  
16 They further allege that Debtor had "total and complete executive  
17 control and power over WC Management and the WC Fund." Debtor  
18 admitted all of these allegations.

### 19 III. CONCLUSION

20 Given that the state court breach of contract claims were  
21 alleged only against WC Funds and not against Debtor, and given  
22 that additional facts supporting the breach of fiduciary duty and  
23 other intentional torts against Debtor were pled separately in the  
24 State Court Complaint, the court concludes that the latter issues  
25 were indeed "necessarily decided" against Debtor by the state  
26 court.

27 Furthermore, in light of Debtor's admissions in this adversary  
28 proceeding that he acted as a fiduciary to WC Funds and the state

1 court's determination that he breached this fiduciary duty, the  
2 court will grant partial summary judgment against Debtor pursuant  
3 to 11 U.S.C. § 523(a)(4). In light of this determination, the  
4 court has not reached the issue of whether the Debtor's obligation  
5 is nondischargeable under 11 U.S.C. § 523(a)(6). If Cadogan  
6 chooses not to pursue the section 523(a)(6) and the section  
7 523(a)(19) claims further, it should dismiss those claims and  
8 submit (and file proof of compliance with B.L.R. 9021-1(c)) an  
9 order granting the MSJ and a separate judgment determining the  
10 state court judgment nondischargeable pursuant to section  
11 523(a)(4). The court will then take the status conference set for  
12 January 26, 2018, off calendar. If Cadogan chooses to pursue the  
13 alternate relief of sections 523(a)(6) or (a)(19), the January 26  
14 status conference will go forward. Counsel for Cadogan should  
15 notify the court and Debtor by noon on January 25, 2018, how  
16 Cadogan wishes to proceed.

17 **\*\*END OF MEMORANDUM DECISION\*\***  
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Court Service List

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